

D.P.U. 94-3A

Application of Commonwealth Electric Company:

- (1) under the provisions of G.L. c. 164, § 94G and the Company's tariff, M.D.P.U. 275, for approval by the Department of a change in the quarterly fuel charge to be billed to the Company's customers pursuant to meter readings in the billing months April, May and June 1994.
- (2) for approval of a Fuel Charge Stabilization Proposal sponsored jointly by the Company and the Attorney General of the Commonwealth. The Proposal is intended to become effective by April 1, 1994 and would establish target maximum fuel charge rates of \$0.06500 per kilowatt hour over a three year period, and \$0.06500 to \$0.06700 per kilowatt hour during the fourth year. Under the terms of the Settlement, the total deferred costs would not exceed \$40 million and would be collected along with carrying costs in the subsequent six year period.
- (3) for approval by the Department of rates to be paid to Qualifying Facilities for purchases of power pursuant to 220 C.M.R. §§ 8.00 et seq. and M.D.P.U. 251. The rules established in 220 C.M.R. § 8.00 set forth the filings to be made by electric utilities with the Department, and implement the intent of sections 201 and 210 of the Public Utilities Regulatory Policies Act of 1978.

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I. INTRODUCTION

On March 3, 1994, pursuant to G.L. c. 164, § 94G and 220 C.M.R. §§ 8.00 et seq., Commonwealth Electric Company ("Commonwealth" or "Company") notified the Department of Public Utilities ("Department") of the Company's intent to file a quarterly change to its fuel charge in conformance with its tariff, M.D.P.U. 275, and to its Qualifying Facility ("QF") power purchase rates in conformance with its tariff, M.D.P.U. 251. The Company requested that both these changes be effective for bills issued pursuant to meter readings for the billing months of April, May and June 1994. The matter was docketed as D.P.U. 94-3A.

On March 4, 1994, the Company and the Attorney General of the Commonwealth ("Attorney General") filed a Fuel Charge Stabilization Settlement proposal ("stabilization proposal"), consisting of an Offer of Settlement ("Offer"), a Joint Motion for Approval of Offer of Settlement ("Motion"), an explanatory letter ("letter") prepared by the Company and supporting schedules. The stabilization proposal requires that Department approval must be granted by April 1, 1994, to coincide with the Company's fuel charge quarter, or the stabilization proposal will be null and void.

¹ Although the parties have captioned their filing a "Settlement", a settlement implies resolution of an actual dispute. Therefore, this matter will be treated as a joint proposal.

The Company's fuel charge filing included two calculations: first, the fuel charge that would result from approval of the stabilization proposal; and second, the fuel charge that would result from the traditional methodology, in the event the Department does not approve the stabilization proposal.

Commonwealth, a wholly owned subsidiary of Commonwealth Energy System ("ComEnergy") serves approximately 258,000 retail customers in 38 cities and towns in southeastern Massachusetts, on Cape Cod and on Martha's Vineyard. ComEnergy is an exempt holding company under the Public Utility Holding Company Act of 1935. ComEnergy's other subsidiaries, affiliates of Commonwealth, include Cambridge Electric Light Company ("Cambridge"), Canal Electric Company ("Canal"),² Commonwealth Gas Company and Commonwealth Energy Service Company ("ComEnergy Service"). Commonwealth operates several small oil/gas-fired generating units and has contractual interests in Pilgrim 1, Yankee Rowe and Point Lepreau nuclear units. The Company also has contractual interests in Canal Unit 1 and Canal Unit 2, two large oil-fired units operated by the Company's affiliate, Canal.

Pursuant to notice duly issued, a public hearing on the Company's application was held on March 25, 1994, at the Department's offices in Boston. Notice of the hearing was published by the Company in the New Bedford Times, the Cape Cod Times and the Boston Globe. The Company also complied with the

² The electric operating subsidiaries are referred to collectively as "ComElectric."

requirement to mail a copy of the notice of the hearing to all persons with whom the Company has special retail contracts that do not incorporate a filed rate, and to notify all intervenors and their respective counsel from the Company's prior two fuel charge proceedings that it was proposing an adjustment to its fuel charge. The Company was also required to inform all intervenors of the date of the public hearing. The Attorney General intervened as of right in this proceeding pursuant to G.L. c. 12, § 11E. The Massachusetts Executive Office of Economic Affairs, Division of Energy Resources petitioned for and was granted intervenor status³. No other party sought leave to intervene; however, the Department received a letter on March 18, 1994, from Save Our Regional Economy ("S.O.R.E.") urging the Department to approve the stabilization proposal.

At the hearing, the Company sponsored three witnesses: John A. Whalen, comptroller for ComEnergy; Charles R. Fox, Jr., senior rate analyst in rate administration at ComEnergy Service; and Michael R. Kirkwood, manager of power supply administration for ComElectric. The Company submitted seven exhibits: the prefiled testimony of Mr. Fox (Exh. CEC-1); schedules in support of Mr. Fox's testimony (Exh. CEC-2); bills and contracts for fuel oil supplies, purchased power and transmission services for December 1993, January and February 1994 (Exh. CEC-3); the prefiled testimony of Mr. Kirkwood (Exh. CEC-4); schedules in

³ The Division of Energy Resources did not appear at or participate in the hearing.

support of Mr. Kirkwood's testimony (Exh. CEC-5); the Fuel Charge Stabilization proposal filed on March 4, 1994 (Exh. CEC-6); and revisions dated March 22, 1994, to the schedules contained in the proposal (Exh. CEC-7). The Company also provided responses to eight Information Requests issued by the Department, which were admitted into evidence as Exhibits DPU-1 through DPU-8.

II. THE COMPANY'S STABILIZATION PROPOSAL

A. Overview

The Company's proposal is designed to stabilize Commonwealth's fuel charge over the next four years, followed by a six year period of recovery of any fuel-related deferred amounts (Exh. CEC-6, letter at 1-2). The Company proposes to cap the fuel charge at 6.5 cents per kilowatt hour ("KWH") for three years, 1994-1996, and at 6.7 cents per KWH for the fourth year, 1997 (Exh. CEC-6, Offer at 1). Any unrecovered fuel-related costs would be deferred during those four years ("deferral period"), and then recovered, with interest charges, over the subsequent six years ("recovery period") id.). The parties negotiated the proposal in response to the highly volatile nature of the Company's fuel charge (Exh. CEC-6, letter at 4). Since January 1990, Commonwealth's fuel charge has ranged from 4.6 cents to 9.1 cents per KWH id.; Exh. CEC-7, Att. 1). Since the decision in the Company's last rate case, in July 1991, its fuel charge has ranged from 4.9 cents to 6.7 cents per KWH id.). The Company attributes this unusual volatility in part to the fact that it experienced one of the highest rates of growth in

sales among New England utilities during the 1980s, requiring the Company to add substantial amounts of new, higher cost generation, followed by significant erosion of sales in the early 1990s due to the regional recession (Exh. CEC-6, letter at 3, n.2).

B. Deferral and Recovery Under the Proposal

No more than \$16 million shall be deferred in any one year, and no more than \$40 million shall be deferred during the first four years (*id.*). If in any quarter during the deferral period, the fuel charge caps would cause either the annual deferral or the total deferral to exceed the \$16 and \$40 million ceilings, then the fuel charge cap for that quarter will be adjusted upward such that the deferral will not exceed either ceiling (Exh. CEC-7, Att. 3). The Company indicated that should such a situation arise, it would consider suspending or terminating the stabilization proposal (Tr. at 51)⁴.

If there is a deferred balance and the Company's quarterly fuel charge is projected at less than 6.5 cents per KWH, the Company shall nevertheless propose a rate of up to 6.5 cents per KWH, and apply the difference between the lower projected rate and the Department approved rate in order to reduce the balance

⁴ The Company is authorized under the terms of the stabilization plan to suspend or terminate the plan at any time the Company determines in its sole judgment that achievement of the fuel charge rate within the range set forth in the stabilization plan is no longer feasible (Exh. CEC-6, Offer at 2).

of any deferred costs (Exh. CEC-6, Offer at 2). If there is no deferred balance, the Company shall propose a rate based on the traditional method (id.).

The Company currently estimates that if it successfully renegotiates some of its contracts, it will defer approximately \$27 million over the deferral period (Tr. at 30; Exh. CEC-7, Att. 2). If not, the projected deferral amount is the full \$40 million (Exh. CEC-7, Att 3).

The stabilization proposal does not include carrying charges as part of the \$40 million deferral amount (Tr. at 28). Interest throughout the deferral and recovery periods is to be calculated at a rate equal to the Bank of Boston prime rate, minus two percentage points, times 150 percent; however, the interest rate will not exceed the Company's overall cost of capital as determined in the Company's most recent rate case (id. at 80). Capping the interest rate at its cost of capital, the Company contends, will help it to maintain its financial ratios and enable continued access to the financial markets (Exh. CEC-6, letter at 8).

C. Treatment of Stranded Deferred Costs

In the event any customer on the Company's Large Industrial Rate G-3 should begin to take at least 50 percent of its power requirements from a source other than the Company at any point during the deferral or recovery period, any unrecovered deferred expense attributable to that customer shall be calculated according to a specific formula, removed from the total

recoverable deferred expenses and absorbed by the Company's shareholders (Exh. CEC-6, Offer at 3). Thus, no other customer will be required to absorb any such stranded deferred costs.⁵ If the customer returns to the system at any point during the deferral or recovery period, a similar formula will be applied to determine a prorated portion of the then-unrecovered deferred amount to be charged to the customer to replace a portion of the unrecovered deferred amount attributable to the customer^{id.}).

D. Bill Impacts

The Company provided estimated bill impacts for years five through ten under two scenarios. First, the Company assumed that it will be successful in renegotiating some of its power-purchase contracts. In this case, recovery of the deferred costs will impact future bills at increasing rates ranging from a low of 0.17 percent for the smallest residential users in year five, to a high of 4.29 percent for the largest industrial customers in year ten, the final year (Exh. CEC-7, Att. 2). Second, the Company assumed that it may be unsuccessful in renegotiating any of its power-purchase contracts. Under this assumption, the parallel bill impacts range from increases of 0.38 percent to 4.59 percent (id., Att. 3).

⁵ The amount of deferred expenses attributable to any customer under this provision of the stabilization proposal shall be based on a pro rata share of total deferred costs, such that a customer's share would be equivalent to that customer's total consumption during the deferral period as a percentage of total system KWH sales during the deferral period (Exh. CEC-6, Offer at 3-4).

E. The Company's Position

The Company asserts that the stabilization proposal, in conjunction with the Company's "rate control plan,"⁶ will eliminate the significant disincentive to economic development and customer hardship presented by a volatile and unpredictable fuel charge (Exh. CEC-6, letter at 9; Tr. at 25).

The Company also states that its supply mix currently contains an unusually high number of newly-executed, front-loaded, long-term power-purchase contracts (Exh. CEC-6, letter at 3). The Company stated that it defines a front-loaded contract as one in which costs associated with the contract in the early years are greater than avoided costs (Tr. at 41). According to the Company, front-loaded contracts cause an inherent intergenerational inequity because ratepayers during the early years of the contracts are subject to rates in excess of avoided costs while ratepayers in later years will be subject to rates lower than avoided costs (Exh. CEC-6, letter at 3). The Company also contends that, because front-loaded contracts require inflated demand payments from current ratepayers for the benefit of future generations of ratepayers, they send inaccurate price signals (id.). The Company argues that the deferral would

⁶ According to the Company, the "rate control plan" is an effort to contain the cost of purchased power and includes re-negotiating price terms, contract buy-outs, and generating-unit shut-downs. The "rate control plan" is not part of the stabilization proposal presently before the Department. The Company stated that it is currently renegotiating some of its contracts (Tr. at 45).

mitigate this intergenerational inequity and address the issue of inaccurate price signals id.).

Finally, the Company asserts that the proposal is both legally sound and consistent with Department practice (Exh. CEC-6, at 4-5, citing Commonwealth Electric Company D.P.U. 91-3B-1 (1991) and Commonwealth Electric Company D.P.U. 93-3B (1993)). The Company claims that the stabilization proposal is completely consistent with the statute in that the only difference between the stabilization proposal and a typical fuel charge is the inclusion of an amount of deferred costs as an adjustment to achieve the stabilized rate (Exh. DPU-8, at 2).

III. FUEL CHARGE

On March 18, 1994, the Company filed with the Department its proposed changes to its fuel charge and QF power purchase rates for April, May and June 1994. As indicated, for these billing months, the Company offers two alternative fuel charges. The first, \$0.06500 per KWH, is made pursuant to and consistent with the stabilization proposal discussed above. This proposed fuel charge is \$0.00149 per KWH less than the fuel charge of \$0.06649 per KWH approved by the Department in Commonwealth Electric Company, D.P.U. 93-3D (1993) pursuant to meter readings for the billing months of January, February and March 1994 (Exh. CEC-1, at 4). In order to achieve the target rate of \$0.06500 per KWH established under the stabilization proposal, this alternative fuel charge reflects a quarterly deferral of \$12.3 million (id. at 6-7).

In the event the Department does not approve the stabilization proposal, the Company proposes a fuel charge rate based on the traditional methodology. This alternative fuel charge would be \$0.08140 per KWH, which is \$0.01491 per KWH more than the fuel charge of \$0.06649 per KWH approved by the Department in the Company's last fuel charge quarter (id. at 9).

The Company offered several reasons for the increase in the fuel charge expenses projected for the upcoming quarter (id. at 6-7). The Company first explained that recoverable costs for the next quarter, excluding any deferral, are projected to be \$1,527,694 more than the recoverable costs included in the Company's previous fuel charge filing Commonwealth Electric Company, D.P.U. 93-3D (1993)⁷. According to the Company, the factors leading to the projected increase in recoverable costs for the upcoming quarter are: (1) an increase of \$706,600 in projected purchased power demand and transmission costs; (2) an increase of \$1,999,894 in the prior period reconciling adjustment; and (3) a reduction of 145,262,000 KWH in billed sales projected over the April-June quarter when compared to the prior quarter (id.). The Company indicated that the primary reasons for the projected increase in purchased power demand and transmission costs are: (1) an increase in costs associated with the SEMASS contract, for which demand charges are a function of unit availability, which has been increasing recently;

⁷ \$12,310,000 - \$10,782,306 = \$1,527,694 (Exh. CEC-1, at 6).

(2) increased operations and maintenance expense related to a scheduled refueling outage at Pilgrim station; and (3) increased costs associated with the Masspower 2 contract, for which contract prices are a function of audited unit output, which has been rising recently (Tr. at 55-56). Partially offsetting these factors is an expected decrease of \$1,178,800 in projected energy costs in the upcoming quarter id. at 6).

IV. QUALIFYING FACILITIES

Pursuant to the Department's rules, 220 C.M.R. §§ 8.00 et seq., rates to be paid to QFs for short-run power purchases are set with the same frequency as the fuel charge. A QF is a small power producer or cogenerator that meets the criteria established by the Federal Energy Regulatory Commission in 18 C.F.R. § 292.203(a) and adopted by the Department in 220 C.M.R. § 8.02.

Pursuant to the governing regulations, the Company is required to calculate short-run energy purchase rates on a time-of-supply basis for two rating periods: peak and off-peak. In addition, the Company is required to calculate a non-time-differentiated rate, i.e., a total period rate, which is a weighted average of the time-of-supply rates, where the weighting is a function of the number of hours in each rating period. See 220 C.M.R. § 8.04(4)(b).

The Company proposed the following standard rates to be paid to QFs during April, May and June 1994:

Energy Rates By Voltage Level (Dollars/KWH)

| <u>Voltage Level</u> | <u>Peak</u> | <u>Off-Peak</u> | <u>Total</u> |
|----------------------|-------------|-----------------|--------------|
| Primary | 0.02048 | 0.01735 | 0.01818 |
| Secondary | 0.02127 | 0.01805 | 0.01891 |

(Exh. CEC-4, Sch. 1, at 1).

Short-Run Capacity Rates (Dollars/KWH)

Voltage Level

| | |
|-----------|---------|
| Primary | 0.04879 |
| Secondary | 0.04962 |

(id. at 9).

V. ANALYSIS AND FINDINGS

The three principal issues presented by the proposal are:
 (1) whether deferring fuel charge expenses beyond the quarter in which they are incurred comports with the intent of the fuel charge statute; (2) whether the proposal is consistent with Department practice and policy; and (3) whether the stabilization proposal is in the public interest.

Under the pertinent statute, G.L. c. 164, §94G (b):

[The] fuel charge may be based on reasonable estimates of the total costs of fuel and power purchased for resale to customers, as appropriate in accordance with the company's fuel charge rate schedule, during the quarter in which the fuel charge shall apply. The burden of proof shall be upon the utility company to demonstrate the reasonableness of energy expenses sought to be recovered through the fuel charge.

The approved fuel charge shall reflect a reconciliation for any differences between the fuel charge revenues and actual fuel and purchased power costs, less zero power costs as defined herein, for the three months preceding the month of

filing as well as estimated differences for the month of filing and all other adjustments determined by the department pursuant to this subsection

Section 94G (e) states:

The Department may ... incorporate the use of any factors in addition to and not inconsistent with factors set forth in this section, in its considerations under any subsection hereof.

In Fitchburg Gas and Electric Light Company D.P.U. 92-5C at 8 (1992), the Department permitted Fitchburg early recovery of future capacity costs associated with its new KES power-purchase contract. More specifically, the Department allowed Fitchburg to gradually phase in the KES capacity costs over the period from August 1992 through January 1993, even though Fitchburg would not begin to incur KES capacity costs until November 1992 Id. at 3. The Department approved the Fitchburg proposal in order to lessen the impact of the KES contract on its fuel charge Id. at 7. The Department noted that Fitchburg's objective of smoothing out costs was in the best interests of its ratepayers Id.

In Commonwealth Electric Company D.P.U. 91-3B-1, at 7 (1991), the Department approved a proposal to defer recovery of a reconciling amount of \$6.0 million from the third quarter to the fourth quarter. The Department noted that the overall reduction in customers' bills was sufficient to address rate continuity concerns. Id.

In Commonwealth Electric Company D.P.U. 93-3B at 3 (1993), Commonwealth proposed a mechanism to levelize its fuel charge over a period of nine months. Commonwealth projected that its

fuel charge during that period would be particularly volatile, primarily due to an increase in costs associated with three capacity contracts. Id. In that case, the Department rejected Commonwealth's proposal to mitigate fuel charge volatility, but approved an adjustment, similar to that in the Fitchburg case, that allowed Commonwealth to phase-in the capacity costs that it would incur under the three contracts in question. D.P.U. 93-3B at 4-5.

Based on the unique circumstances of the Company, in particular, the highly volatile fuel charge experienced by the Company, the large number of front-loaded contracts in the Company's supply mix and resulting intergenerational inequity, the Department concludes that the Company has provided sufficient support for the stabilization proposal. The Department finds that the stabilization proposal is not inconsistent with the intent of the fuel charge statute, with Department practice or policy, and that the proposal is in the public interest.

Based on the foregoing, the Department finds:

1. that the fuel charge to be applied to Company bills issued pursuant to meter readings for the billing months of April, May and June 1994, shall be \$0.06500 per KWH. (The calculation of the fuel charge is shown in Table 1 attached to this Order.)

2. that the qualifying facility power purchase rates for April, May and June 1994, shall be the rates set forth in Section IV above.

3. that the stabilization proposal is not inconsistent with the intent of the fuel charge statute, Department practice or policy, and is in the public interest.

VI. ORDER

Accordingly, after due notice, hearing and consideration, it is

ORDERED: That the Fuel Charge Stabilization Settlement proposal be and hereby is approved, effective on and after April 1, 1994.

FURTHER ORDERED That Commonwealth Electric Company is authorized to put into effect a quarterly fuel charge of \$0.06500 per KWH pursuant to the stabilization proposal and as set forth in Section V, Finding 1 of this Order for bills issued pursuant to meter readings for the billing months of April, May and June 1994, subject to refund; and it is

FURTHER ORDERED That the fuel charge approved herein shall apply to kilowatthours sold to the Company's customers subject to the jurisdiction of the Department and shall be itemized separately on all such customers' electric bills; and it is

FURTHER ORDERED That the Company's Qualifying Facility power purchase rates for the billing months of April, May and June 1994, shall be those set forth in the Table on Page 12 of this Order; and it is

FURTHER ORDERED That the Company, in all future fuel charge proceedings, shall notify all intervenors and their respective counsel from the Company's prior two fuel charge proceedings that

it is proposing an adjustment to its fuel charge, and shall also notify these persons of the date scheduled for the hearing on the proposed fuel charge at least ten days in advance of the hearing; and it is

FURTHER ORDERED That the Company, in all future fuel charge proceedings, shall provide all intervenors and their respective counsel from the prior two fuel charge proceedings with a copy of its fuel charge filing, in hand or by facsimile, on the same day it is filed with the Department; and it is

FURTHER ORDERED That, pursuant to G.L. c. 164, § 94G (a) and (b), fuel costs allowed by this Order are subject to such disallowance as the Department may determine in any subsequent investigation of the Company's performance period that includes the quarter applicable to the present charges.

By Order of the Department,